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No. 88-1723

In the Supreme Court of the United States

OCTOBER TERM, 1988

ARCHER-DANIELS-MIDLAND COMPANY, ET AL.,
PETITIONERS

v.

UNITED STATES OF AMERICA

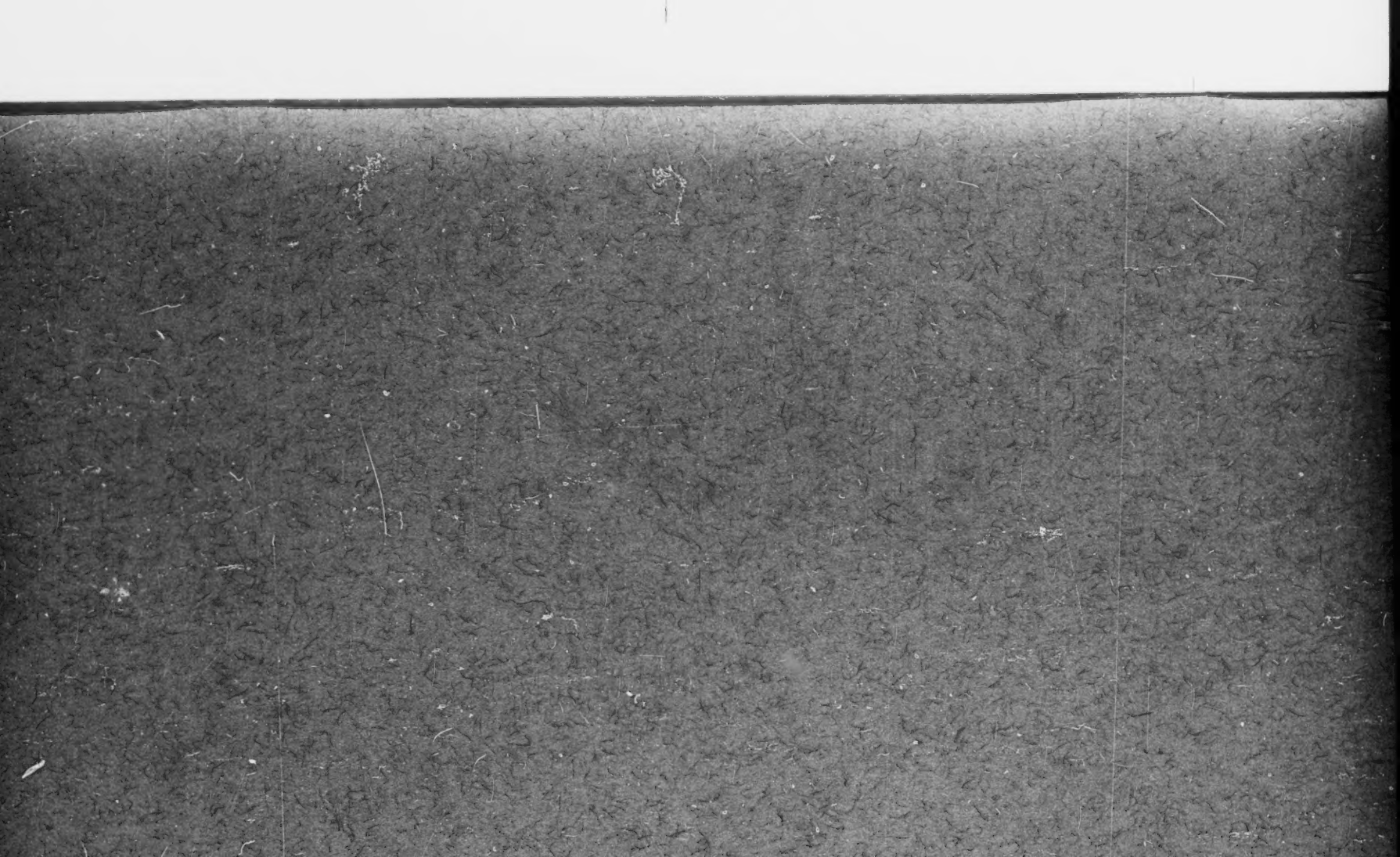
ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

KENNETH W. STARR
Solicitor General
JUDY L. WHALLEY
Acting Assistant Attorney General
BRIAN J. MARTIN
Assistant to the Solicitor General
ROBERT B. NICHOLSON
DAVID SEIDMAN
Attorneys

Department of Justice
Washington, D.C. 20530
(202) 633-2217

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QUESTION PRESENTED

Whether the court of appeals erred in holding that sugar and high fructose corn syrup are not in the same relevant market for the purpose of examining a merger under the antitrust laws.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-12a) is reported at 866 F.2d 242. The opinion of the district court (Pet. App. 13a-54a) is reported at 695 F. Supp. 1000.

JURISDICTION

The judgment of the court of appeals (Pet. App. 55a) was entered on December 15, 1988. A petition for rehearing was denied on March 8, 1989 (Pet. App. 56a). The petition for a writ of certiorari was filed on April 24, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. In June 1982, petitioner Archer-Daniels-Midland Company, a leading producer of high fructose corn syrup (HFCS), acquired by long-term lease two plants from petitioner Nabisco Brands, Inc. that were used for producing HFCS. Three months later, the government brought this action claiming that the transaction would diminish competition in the production and sale of HFCS, in violation of Section 7 of the Clayton Act (15 U.S.C. 18) and Section 1 of the Sherman Act (15 U.S.C. 1). The issue raised by the petition for certiorari is whether HFCS and sugar are in the same relevant product market for purposes of analyzing petitioners' transaction under the antitrust laws.

2. Sugar, which comes from cane and beets, has historically been the principal sweetener in foods. Sugar is used by food processors in both its liquid and non-liquid forms. HFCS is a liquid sweetener produced from corn.[1] It is widely used today instead of sugar as a sweetener in many products, most notably soft drinks. Pet. App. 2a. Although HFCS is not suitable for many uses of sugar, sugar is "interchangeable for virtually every use of HFCS" (Pet. App. 38a).

HFCS is cheaper than sugar in the United States. The district court noted that "since its commercial introduction in the 1970's, HFCS has been priced generally at a discount of 10% to 30% below the price of sugar" (Pet. App. 39a). That price difference exists primarily because of the "U.S. Sugar Program," which protects domestic sugar from low-

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[1] HFCS is generally available in three grades: HFCS-42, HFCS-55, and HFCS-90. The number indicates the percentage of fructose in the formulation; the higher the percentage, the sweeter the product. Pet. App. 2a.

priced foreign competition and insulates domestic sugar from low world sugar prices (*id.* at 3a).[2] As the district court stated: "The parties to this litigation agree that the current U.S. Sugar Program has artificially inflated the price of sugar, and as a result, the domestic price of sugar has been higher than the price of HFCS" (*id.* at 24a).

Because HFCS is cheaper than sugar, food processors have gradually switched from sugar to HFCS in circumstances where HFCS is suitable (Pet. App. 7a, 39a-40a). That process has extended over a number of years; the last major step was in 1984 when the major soft drink manufacturers decided to permit complete substitution of HFCS for sugar in their formulations (*id.* at 45a & n.38). As a Department of Agriculture agricultural economist explained (C.A. App. 907-908): "The market for HFCS is now almost completely mature, in the sense that there is only a marginal amount of sucrose [sugar] use left for which HFCS is technically suitable but has not yet displaced sucrose * * *. The process by which HFCS has displaced sugar is therefore largely at an end." As long as the price of sugar is artificially inflated, it is unlikely that this process will be reversed. "HFCS purchasers will not switch back to sugar as long as HFCS remains cheaper" (Pet. App. 4a; see *id.* at 47a-48a).

3. In the district court, the government claimed that petitioners' merger transaction would diminish competition

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[2] The Sugar Program has been in effect since 1934. As petitioners note (Pet. 7), there have been brief periods without effective price support from the U.S. Sugar Program. Those times were periods when market prices for sugar were unusually high (Pet. App. 21a-22a). The current program relies on non-recourse loans and a system of fees and quotas on raw sugar imported into the United States. By its terms, the current program expires with the 1990 crop year, and so its impact on sugar prices will continue at least into 1991.

in the HFCS market. After four years of discovery, petitioners moved for summary judgment on the ground that the government could not prove that HFCS was a relevant product market by itself.[3] The district court granted petitioners' motion. The court ruled that the relevant product market included at least sugar in addition to HFCS. Pet. App. 14a.

The court considered three factors in its market analysis: interchangeability of use, cross-elasticity of demand, and price correlation (Pet. App. 30a). The parties agreed that HFCS and sugar were functionally interchangeable in the sense that sugar could be used instead of HFCS. The court found "cross-elasticity of demand between HFCS and sugar" (*id.* at 41a) because "the reduced price for HFCS as compared to sugar has led to substantial displacement of sugar" (*id.* at 39a). In addition, the court noted that in Canada, which has no counterpart to the U.S. Sugar Program, buyers switch back and forth between HFCS and sugar in accordance with changes in the relative prices (*id.* at 40a-41a). The district court then found "significant price correlation between HFCS and sugar" (*id.* at 43a). Lastly, the court stated that "price differentials, even substantial ones, are insufficient as a matter of law to overcome other undisputed evidence showing interchangeability, cross-elasticity and price correlation between substitute products" (*id.* at 46a).

4. The court of appeals reversed. Relying on *United States* v. *E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956) (*Cellophane*), the court stated that the "lawfulness of an acquisition turns on the purchaser's potential for creating,

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[3] The government conceded that, if the relevant product market included sugar, the lease transaction in this case would not significantly diminish competition.

enhancing, or facilitating the exercise of market power – the ability of one or more firms to raise prices above competitive levels for a significant period of time" (Pet. App. 6a). Turning to the record, the court observed that the price of sugar was "artificially inflated" and that buyers had turned to HFCS because of its lower price (*id.* at 7a). It concluded that "[a]s long as an effective price support program is in existence, a monopolist of HFCS will be able to raise the price of HFCS to just below the supported price of sugar before being constrained by the competitive forces of sugar. In other words, the HFCS monopolist is able to exercise excess market power" (*ibid.*). The court concluded, therefore, that although sugar and HFCS are similar in quality, the artificially high price of sugar prevents it from being reasonably interchangeable by consumers with HFCS so they are not in the same relevant product market.

The court of appeals also stated that "[w]hether two particular products belong in the same relevant product market can be demonstrated by the extent of cross-elasticity of demand between the two products; in other words, the readiness and ability of consumers of one product to turn to the other product" (Pet. App. 11a).[4] To show that two products belong in the same market, the cross-elasticity must be sufficiently high so that "a slight increase in the price of HFCS causes a considerable number of buyers of HFCS to switch to sugar" (*id.* at 11a, 12a, n.1). The court of appeals found that "no evidence exists at the present

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[4] Cross-elasticity of demand measures "the extent to which small changes in the current price of one product affects demand for another product." L. Sullivan, *Handbook of the Law of Antitrust* 54 (1977). For a more technical definition, see C. Ferguson, *Microeconomic Theory* 55 (1966).

time demonstrating a high cross-elasticity of demand between sugar and HFCS" (*id.* at 11a).[5]

ARGUMENT

The court of appeals' decision is correct and it does not conflict with any decision of this Court or any other court of appeals. Thus no further review is warranted.

1. a. Section 7 of the Clayton Act prohibits any acquisition whose effect "may be substantially to lessen competition, or to tend to create a monopoly." 15 U.S.C. 18. The lawfulness of an acquisition thus turns on its potential for creating or enhancing the exercise of monopoly power – *i.e.*, the ability to raise prices above competitive levels for a significant period of time. *Cellophane*, 351 U.S. at 391, 393. And "[w]ithout a definition of [the relevant] market there is no way to measure [the] * * * ability [of the challenged transaction] to lessen or destroy competition." *Walker Process Equipment, Inc.* v. *Food Machinery & Chemical Corp.*, 382 U.S. 172, 177 (1965). Accordingly, the central issue in this case is the proper definition of the relevant market.[6]

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[5] The court explained that the district court, in relying on evidence of past displacement resulting from the lower price of HFCS, had mistakenly addressed static, rather than dynamic, price and demand relationships. And the Canadian evidence was irrelevant because "market conditions in Canada differ radically from the market conditions in the United States" (Pet. App. 12a n.1) and would continue to do so as long as the U.S. Sugar Program exists.

[6] When the relevant market is defined, a transaction's probable effect on competition is evaluated by, among other things, the concentration of firms within that market. *United States* v. *Philadelphia National Bank*, 374 U.S. 321, 363 (1963).

In *Cellophane*, this Court outlined the basic approach to market definition.[7] In that case, the government had charged the dominant producer of cellophane with monopolizing the cellophane market. The issue before the Court was whether cellophane itself constituted a relevant product market, or whether other flexible packaging materials were also part of the market (351 U.S. at 399). The Court ruled that the market issue turned on whether competition from other flexible packaging materials constrained the cellophane maker's "power to set the price of cellophane" (*id.* at 392). In particular, the Court focused on whether the various packaging materials were "reasonably interchangeable by consumers for the same purpose" (*id.* at 395) in light of their "price, use and qualities" (*id.* at 404). And the Court examined the various products and observed that customers were very sensitive to price changes – *i.e.*, an increase in the price of cellophane would shift enough purchases to other products to make the price increase unprofitable. The Court held, therefore, that the relevant market included all flexible packaging materials, not just cellophane. *Ibid.*[8]

b. The court of appeals in this case followed the Court's *Cellophane* analysis. It approached the issue of market definition by inquiring into power over the price of

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[7] *Cellophane* involved Section 2 of the Sherman Act, not Section 7 of the Clayton Act. But this Court has relied on the *Cellophane* approach to market definition in Section 7 cases. See, *e.g.*, *United States* v. *Continental Can Co.*, 378 U.S. 441, 449 (1964).

[8] The Court alternatively phrased the question of reasonable interchangeability in terms of cross-elasticity of demand. 351 U.S. at 394, 400. The Court stated that high cross-elasticity of demand between two products indicates that they compete in the same market. 351 U.S. at 400. The Court had made substantially the same point in *Times-Picayune Publishing Co.* v. *United States*, 345 U.S. 594, 612 n.31 (1953).

a single item – here HFCS. The court of appeals used the concepts of reasonable interchangeability and cross-elasticity of demand to determine the boundaries of the relevant product market. The court concluded, on the undisputed facts before it, that the cross-elasticity of demand between sugar and HFCS was low; a small increase in the price of HFCS would not cause a considerable number of buyers of HFCS to switch to sugar. The court of appeals reasoned, therefore, that the two products were not reasonably interchangeable by consumers.[9]

Petitioners contend (Pet. 12-14) that the specific results in *Cellophane* and this case are inconsistent. That claim is unpersuasive. In *Cellophane*, the Court found that products of different prices were in the same relevant product market. But in that case, the difference in price was a function of quality differences. 351 U.S. at 396-399. In other words, the typical consumer would be willing to pay more for the product of higher quality. In this case, by contrast, the difference in price between sugar and HFCS is primarily the result of the U.S. Sugar Program, not quality differences.[10] Sugar and HFCS are functionally interchangeable

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[9] Because the court found low cross-elasticity of demand and an absence of reasonable interchangeability, it did not hold, as petitioners claim (Pet. 11), that "a government price support program provides an exception to the usual antitrust rule that a price differential, without more, does not create separate markets for the two products involved."

[10] Petitioners' claim that all "the price differences reflect actual or perceived quality differences" (Pet. 19) is belied by the record. The undisputed fact is that the U.S. Sugar Program artificially inflates the price of sugar above that of HFCS (see Pet. App. 24a). In the district court, petitioners did not claim that supposed quality differences accounted for the price difference. Compare petitioners' statements at C.A. App. 133-137, 1199-1202 with the government's observation at

products for all uses of HFCS. Accordingly, price alone is the determinative factor in consumer choice and a monopolist of HFCS could raise its price up to the price of sugar.

This case is therefore similar to *United States* v. *Aluminum Company of America*, 377 U.S. 271 (1964), where this Court held that insulated aluminum and insulated copper cable were in different product markets.[11] Although there were no quality differences between the two products, copper cable was more expensive. *Id.* at 276. That price difference, which resulted from differences in material costs (*id.* at 275), led to the displacement of copper by aluminum cable and was decisive in the Court's market definition. The Court stated: "[T]o ignore price in determining the relevant line of commerce is to ignore the single, most important, practical factor in the business" (*id.* at 276). Likewise, because sugar and HFCS are similar in quality in those uses for which HFCS is suitable, the difference in price is critical to market definition here.[12]

C.A. App. 1506. Petitioners' claim first surfaced in its petition for rehearing in the court of appeals.

[11] Although the Court phrased its analysis in terms of submarkets, 377 U.S. at 276, a "submarket" must, for antitrust purposes, satisfy the ordinary criteria of market definition. See, *e.g.*, *Rothery Storage & Van Co.*v. *Atlas Van Lines, Inc.*, 792 F.2d 210, 218 & n.4 (D.C. Cir. 1986), cert. denied, 479 U.S. 1033 (1987); *White & White, Inc.* v. *American Hospital Supply Corp.*, 723 F.2d 495, 502 (6th Cir. 1983).

[12] The cause of the large price difference – a government program – is "simply * * * another fact of market life." *International Telephone & Telegraph Corp.* v. *General Telephone & Electronics Corp.*, 518 F.2d 913, 935-936 (9th Cir. 1975). The possible expiration of the Sugar Program in 1991, at the end of the 1990 crop year, may bring future changes in market conditions. That possibility, however, does not affect market definition now.

2. Contrary to petitioners' contention (Pet. 14-16), the decision below does not conflict with the decisions of other courts of appeals. Petitioners identify several cases in which products were found to be in the same market even though they had different prices. Those cases, however, are all explained on the basis of facts that are not present here.

The district court in *American Crystal Sugar Co.* v. *Cuban-American Sugar Co.*, 152 F. Supp. 387 (S.D.N.Y. 1957), aff'd, 259 F.2d 524 (2d Cir. 1958), ruled that cane sugar and beet sugar were within the same relevant market even though the list price of cane sugar was slightly higher -- *i.e.*, two-tenths of a cent per pound, or a two percent price difference. *Id.* at 402. The district court noted that "[t]o some extent cane sugar has a higher degree of consumer acceptance" (*id.* at 398). That fact might have accounted for the willingness of wholesalers to pay a little more for cane sugar. But in any event, there was evidence that the price difference was fading or even gone in some areas. See 259 F.2d 524, 529-530 (2d Cir. 1958). The district court concluded, therefore, that cane and beet sugar were within the same market because they were "interchangeable and [were] purchased on the basis of price" (152 F. Supp. at 398). That ruling was not challenged on appeal. See 259 F.2d at 527 & n.3, 529. Thus nothing in *American Crystal Sugar Co.* is contrary to the decision in this case, where the price difference is 10 to 30% and where there is no perceived difference in quality with respect to HFCS applications.

The Second Circuit's decision in *Nifty Foods Corp.* v. *Great Atlantic & Pacific Tea Co.*, 614 F.2d 832 (1980), is also consistent with this case. The plaintiff contended in that case that private label waffles and brand name waffles were in different submarkets because of the higher cost of brand name waffles (614 F.2d at 840). But there was no

evidence in that case that the difference in price was due to anything other than usual consumer preference for name brands. Moreover, the court of appeals noted that there was no evidence concerning what effect a change in the price of private label waffles would have on the demand for brand name waffles. Here, by contrast, the court of appeals noted that a small increase in the price of HFCS would not affect the demand for sugar. See Pet. App. 11a. And the difference in prices of HFCS and sugar is not a function of consumer preferences; it is primarily a function of the U.S. Sugar Program. See Pet. App. 24a.

The other cases that petitioners cite (Pet. 14-15) also do not conflict with the court of appeals' decision. In *George R. Whitten, Jr., Inc.* v. *Paddock Pool Builders, Inc.*, 508 F.2d 547, 552 (1st Cir. 1974), cert. denied, 421 U.S. 1004 (1975), the court held that two types of recirculating systems for swimming pools were in the same market where "there are no constant or predictable price distinctions between the two systems" and the relevant elasticity "is high indeed." In *Liggett & Myers, Inc.* v. *FTC*, 567 F.2d 1273, 1274 (4th Cir. 1977), the court merely held that two kinds of dog food with distinct differences in quality and price were in the same product market; it did not address whether the two would have been in the same market had there been no significant difference in quality but nevertheless a substantial difference in price. And in *Kaplan* v. *Burroughs Corp.*, 611 F.2d 286, 292 (9th Cir. 1979), cert. denied, 447 U.S. 924 (1980), the court rightly observed that "price differential alone does not govern the scope of the relevant market" because a court must address – as the court of

appeals did here – consumer responses to price changes and the cross-elasticity of demand.[13]

CONCLUSION

The petition for a writ of certiorari should be denied.
Respectfully submitted.

KENNETH W. STARR
Solicitor General
JUDY L. WHALLEY
Acting Assistant Attorney General
BRIAN J. MARTIN
Assistant to the Solicitor General
ROBERT B. NICHOLSON
DAVID SEIDMAN
Attorneys

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[13] Petitioners suggest (Pet. 16-17) that this Court should resolve a supposed conflict within the Eighth Circuit. Not a single judge of that Circuit perceived any conflict warranting rehearing (Pet. App. 8a-11a, 12a, 56a). And in any event "[i]t is primarily the task of a Court of Appeals to reconcile its intern[illegible] difficulties." *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957) (per curiam).

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